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DEPT FOR NEA/MAG - MNARDI AND JPATTERSON

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TAGS: PGOV PREL ECON EINV AG EG
SUBJECT: ORASCOM TELECOM ALGERIE DISPUTE CAUSES WIDESPREAD
CONTROVERSY

REF: CAIRO 185 AND PREVIOUS

Classified By: Classified By: Ambassador David D. Pearce. Reasons: 1.
4 (b), (d)

SUMMARY

¶1. (C) Orascom Telecom Algerie (OTA), Algeria's largest wireless phone company -- one of the largest and most economically productive foreign investments this decade -- has been assessed USD 650 million in back taxes via a series of assessments dating back to late 2008. On the face of it, many of these assessments appear to be a violation of Algerian laws exempting new foreign investments from taxes for the first few years. OTA, a subsidiary of Egypt-based Orascom Telecom Holding, may not repatriate dividends while its tax dispute remains unresolved. The Embassy has met with OTA and Egyptian Embassy officials to determine the true nature of this dispute. More recently, OTA actions have raised questions about its intentions, and rumors are circulating anew that the company is actively looking to sell out. OTA and a number of observers believe that nothing less than OTA's demise or departure from the Algerian market will suffice for the GOA, which seems to have no intention to relent on the fine it has levied. This dispute appears to have started as an economically nationalist reaction to the company's success and repatriation of profits amounting to several hundred million dollars but has become a more intractable dispute thanks to recent tensions between Algiers and Cairo. Above all else, it has emerged as the most publicized recent major dispute involving foreign holdings to tarnish Algeria's already cloudy investment climate. END SUMMARY.

Background

¶2. (U) Orascom Telecom Holdings (OTH) is an international telecommunications company registered in Egypt that operates GSM networks in the Middle East, Africa, and Asia. Orascom Telecom Algerie (OTA), the Algerian subsidiary of OTH, is Algeria's largest mobile telephone provider, operating under the "Djezzy" brand. OTA is 98.6 percent owned by OTH and 3.2 percent by local Algerian investors. Post understands that there is significant U.S.-based investor participation in OTA through a number of investment companies. In July 2001, OTH won an auction for the second GSM license in Algeria, paying USD 737 million and receiving tax exemptions covering OTA's initial five years of operations as well as investment protections granted under Algerian and international law. Local company representatives tell the Embassy that OTA then invested several billion dollars building a wireless network.

¶3. (U) That network has since become the largest network in

the country, providing wireless coverage to 99 percent of the population, bringing Algeria into the late 20th century in terms of wireless and generating significant revenue and profit for the company. In November 2009, however, OTA was assessed tax arrears of approximately USD 600 million for the tax years 2005 through 2007, following an assessment in 2008 of USD 50 million for the tax year 2004. OTA may not repatriate profits while the assessment remains unresolved, and it has had to deposit a quarter of the disputed tax amount with the GOA pending resolution of the case. The amount of profits currently unrepatriated stands at more than USD 250 million.

¶4. (U) On December 28, 2009, OTH announced that OTA had filed an administrative appeal against the November reassessment received from the Algerian Direction des Grandes Entreprises (DGE) for the 2005, 2006, and 2007 tax years. On January 4, Algerian newspaper "El Watan" reported that a source close to the Algerian Ministry of Finance estimated that the dispute would take four to six months to resolve. Algerian law requires a government dispute commission to complete its review of Orascom's complaint within four months. The tax authorities would then have two months to consider the commission's findings and make a final determination.

OTA Perspective

¶5. (C) On January 5, DCM, Econoff, and FCS met with the Director General of Djezzy, Tamer Mahdi, an Egyptian national, to discuss Orascom's tax dispute. Despite OTA's 2004-2007 tax exemptions granted to new foreign investors, Mahdi confirmed that the tax authority (Direction General des Impots - DGI) was reviewing the company's revenues. Mahdi explained that the DGI assessment for 2004 revenues resulted from accounting errors and different standards applied by OTA and the GOA. This led to an initial tax assessment of USD 50 million in 2008 that OTA has appealed. The tax authority subsequently extrapolated from the additional revenues it uncovered for 2004 to claim that OTA failed to declare all of its revenue for 2005-2007 and was stealing from shareholders (a charge OTA vigorously rejects). The DGI assessed back taxes of USD 600 million for this alleged infraction. Mahdi confirmed that OTA appealed the 2005-2007 assessment and made a payment covering 20 percent of the disputed amount. This latter appeal may take eight months or longer, while a decision on the 2004 assessment (for which OTA had earlier made an initial payment and filed an appeal) is scheduled for the March/April timeframe. Mahdi said he raised Orascom's complaint with Finance Minister Karim Djoudi and has invited the government to examine Orascom's financial records. For now, Orascom plans to follow the dispute process established by Algerian law. The GOA, meanwhile, shows no intention of backing down or compromising on a settlement. (Note: OTA CEO Mahdi stopped by the Embassy February 2 and dropped off a packet of documents with the Commercial Attache at the Embassy entrance but refused to exchange words and quickly departed. The packet contained a company legal brief stating OTA's understanding of the facts of the case, copies of OTA correspondence with the MFA and the GOA "Direction of Large Enterprises," and an unsigned letter on plain paper purportedly from TA Associates and Madison Dearborn addressed to "His/Her Excellency" (no further addressee) requesting that that person write President Bouteflika or Prime Minister Ouyahia asking for help resolving the tax dispute. End note)

Egyptian Perspective

¶6. (C) On January 12, DCM and Econoff had a working lunch with Egyptian Embassy then-Charge d'Affaires Hesham Abdel Wahab and Commercial Officer Ismail Khozayem to discuss the OTA case and the current state of Algerian-Egyptian relations. The Egyptians placed the tax dispute in the framework of tensions in Algerian-Egyptian relations, aggravated by the bad feeling over the November 2009 World

Cup soccer qualifying matches. Wahab informed us that Algerian officials suspected an employee associated with OTA is related to President Mubarak and that Algeria is using the company and the tax problems to "cause harm" to the Egyptian president. Egypt's foreign minister has sent an official letter to the Algerian government stating his concerns, but there has been no response. Wahab believed the Algerians will not respond until the Egyptian Ambassador returns to Algeria. (Note: The Egyptian Ambassador left Algiers in November in the aftermath of the November soccer fallout. He returned the week of February 1. End note)

¶7. (C) Wahab did not believe the Algerians would compromise on OTA's tax obligations, even at the risk of driving OTA out of business and doing even greater harm to Algeria's image as an investment destination. He believed that current poor relations between Cairo and Algiers would only complicate efforts to reach a settlement. On a slightly brighter note, Wahab said that tensions between Algeria and Egypt had slightly eased in recent weeks, and most of the estimated 8,000 Egyptian residents in Algeria who had fled in the wake of soccer-fueled violence had returned. Most Egyptian businesses were operating without incident, and trade was largely untouched, but the Algerians canceled a munitions precursor contract worth several million dollars for no apparent reason. (Note: the atmosphere leading up to and following the January 28 Africa Cup game between Algeria and Egypt was far calmer than in November, with the press unanimously blaming Algeria's 4-0 defeat on a biased referee. End note)

¶8. (C) On February 9, Egyptian Political Counselor Tomoum told us that Cairo had not instructed his embassy to intervene on behalf of OTA. Tomoum understood that Orascom headquarters in Cairo was deliberating on further steps but for now was focused on negotiating a solution with Algerian tax authorities. A market intelligence analyst, meanwhile, told the DCM on February 10 that a hedge fund he represents with a huge stake in OTA had asked him to assess prospects for a settlement of the tax fine. His conclusion is that such prospects are extremely grim, as the GOA seems to have decided to force OTA out of the Algerian market. His view was that OTA's incompetent local management had committed a number of misdeeds and missteps that upset Algerians, including the refusal to open the company up to local investors. More fundamentally, however, OTA's sloppy bookwork had left it exposed to exactly the sort of scrutiny and legal action it was facing. He has heard that OTA is trying to sell out but frustrated that it cannot get the USD 10 billion it thinks the company is worth (current assessed value is closer to USD 4-5 billion). He says that thoughts about offering shares on the Algerian stock market are too little, too late, but a Spanish telephone company is reportedly coming forward with a strong interest in taking on OTA's holdings.

¶9. (U) The Algerian newspaper "El Watan" on February 17 highlighted an interview Orascom Telecom Holding's CEO, Naguib Sawiris, gave to the "Wall Street Journal" (and reported in that paper's February 15 edition) to the effect that his company would sell its Algerian operations if it receives a "clear sign its investment (there) isn't welcome." Sawiris stressed OTH's desire to remain in Algeria but "wouldn't hesitate to sell" if the current tax dispute became too serious, and he claimed there was "considerable" interest by other buyers to acquire OTA's assets. In addition, Sawiris maintained he had opted not to escalate by invoking OTA's right to seek international arbitration and that OTA had sufficient cash to operate for two more years. The "El Watan" article cited an anonymous Algerian official source who reportedly told Reuters that Sawiris was "intelligent enough to understand it is time for his company to leave the Algerian market. ...We don't want Orascom any more." The same source speculated that the GOA would not explicitly force Orascom to leave but would resort to indirect pressure until it pulled out.

Comment

¶10. (C) The OTA dispute has become a prime example of the real problems facing foreign business operating in Algeria, given the GOA's historically suspicious attitude toward foreign investors and tendency to adopt measures against their interests without prior consultation or warning. OTA's situation is dramatic but not unique, as we have seen this pattern in other investment disputes. OTA's current problems are doubtless more acute given the unhappy recent history of other Orascom subsidiaries operating in Algeria, including one that spurred the quick march toward economic nationalism a few years ago over allegedly predatory business practices and decisions that wounded Algerian amour propre. The deterioration of Algerian/Egyptian relations over World Cup soccer qualification intensified the focus on OTA, considered an Egyptian company, but did not alone make it a target. Thanks, however, to the still poor state of Algerian/Egyptian relations, the prospects for an amicable settlement of the OTA dispute are currently not bright. If relations mend, chances for a quiet settlement could increase but only if the Algerians would agree, uncharacteristically, to back down.

¶11. (C) As with other commercial disputes in Algeria, it is hard to discern what is going on, who is involved, and the real motives at play. OTA's CEO and other contacts suggest PM Ouyahia is orchestrating this campaign in his guise as the "enemy of success" for any company whose revenue exceeds a certain level and is not protected by President Bouteflika. Whatever may be going on politically behind the scenes, it does look increasingly as though the GOA intends to drive OTA out without any regard for the billions of dollars it invested here, the stimulus to development from the extensive Djezzy wireless network, or the inevitable damage the company's demise would inflict on Algeria's already troubled reputation as an investment destination.
PEARCE